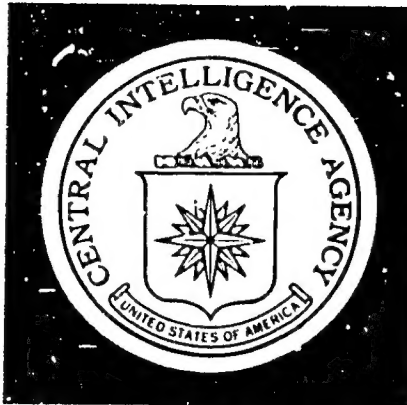


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DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

*Singapore: Some Economic Implications
of the UK Military Withdrawal*

Secret

ER IM 68-131
October 1968

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
October 1968

INTELLIGENCE MEMORANDUM

Singapore:
Some Economic Implications
of the UK Military Withdrawal

Summary

By 1971, Singapore will have to plan and implement measures to compensate for the loss of the British military establishment whose bases occupy 12 percent of the island's total land area, generate 20 percent of gross domestic product (GDP), and provide direct employment for 54,000 of Singapore's 2 million people. Singapore is making a determined effort to minimize this considerable blow to its economy. During the four-year transition period, government spending is planned to increase by \$312 million (including \$120 million in loans and grants from the British), the large naval base and probably the airbases will be converted to civilian use, and private investment will be encouraged in tourism and manufacturing. These factors and the basic strength of Singapore's economy should enable the island to make the transition without serious economic consequences.

The withdrawal comes at a time when the economy of Singapore is expanding rapidly, as the result of an aggressive government program to industrialize as well as a substantial inflow of foreign capital. Singapore's economy has been shaken twice previously in the 1960's: in 1963 because of Indonesia's policy of confrontation with Malaysia and again in 1965 when Singapore opted out of the Federation with Malaysia. Despite these setbacks, Singapore's GDP has grown at a rate of 9 percent a year since 1960. Even with this

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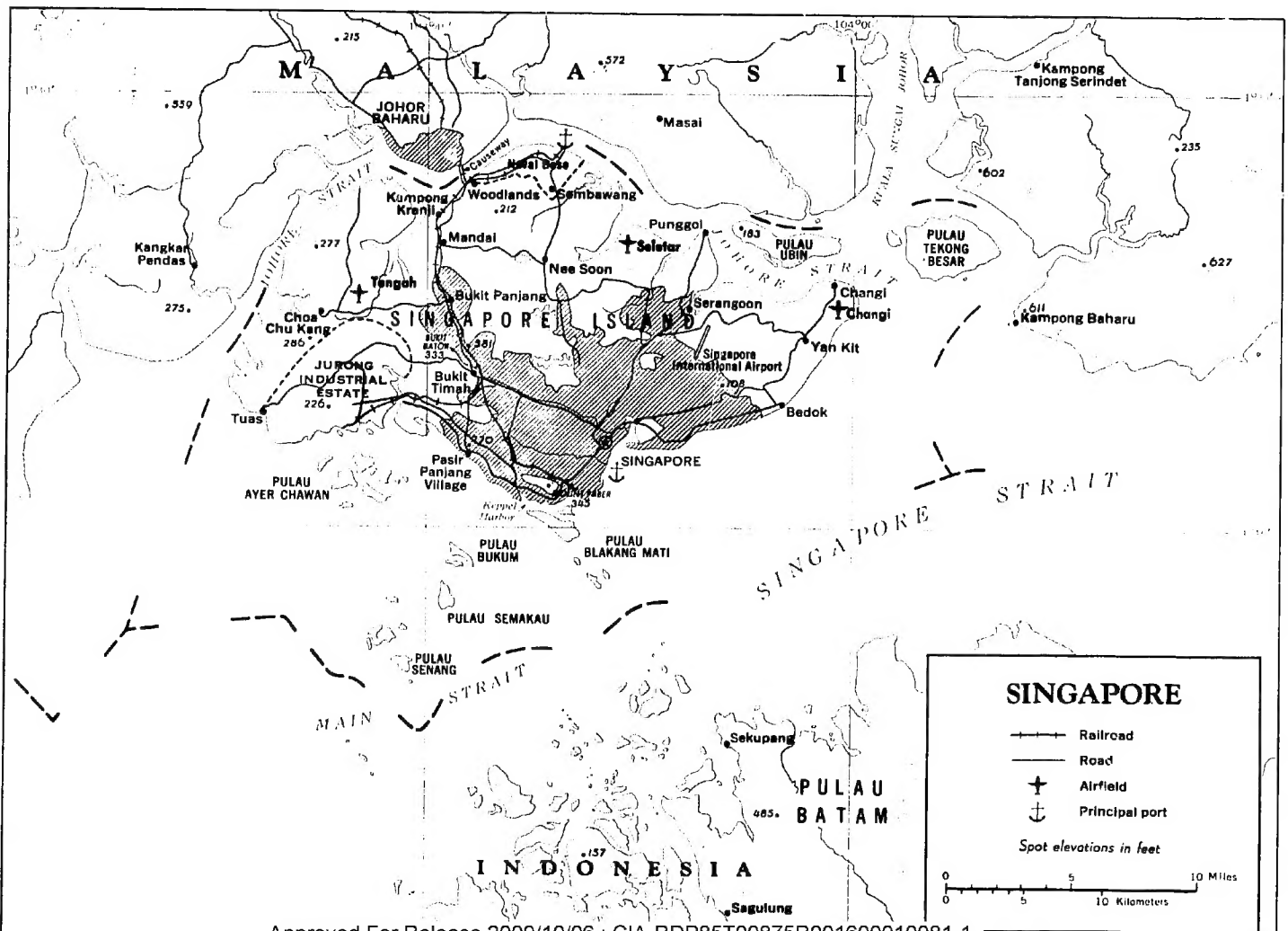
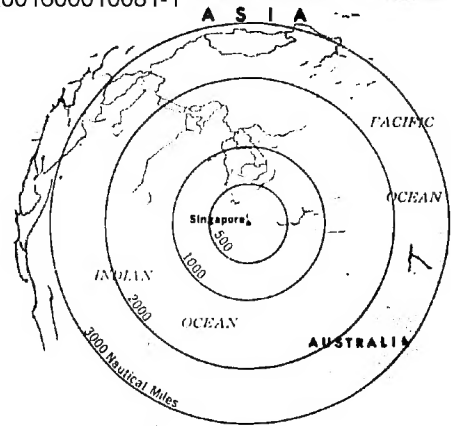
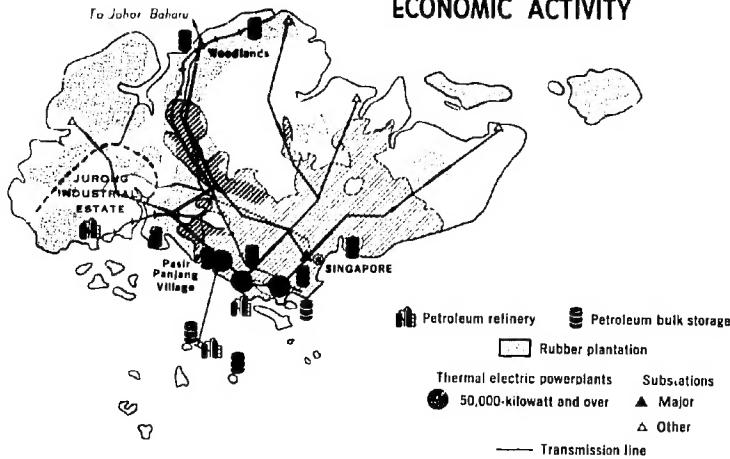
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rate of expansion, however, the economy in the past has failed to provide enough jobs for the growing labor force, leading to an increase in unemployment which has become the island's major economic problem.

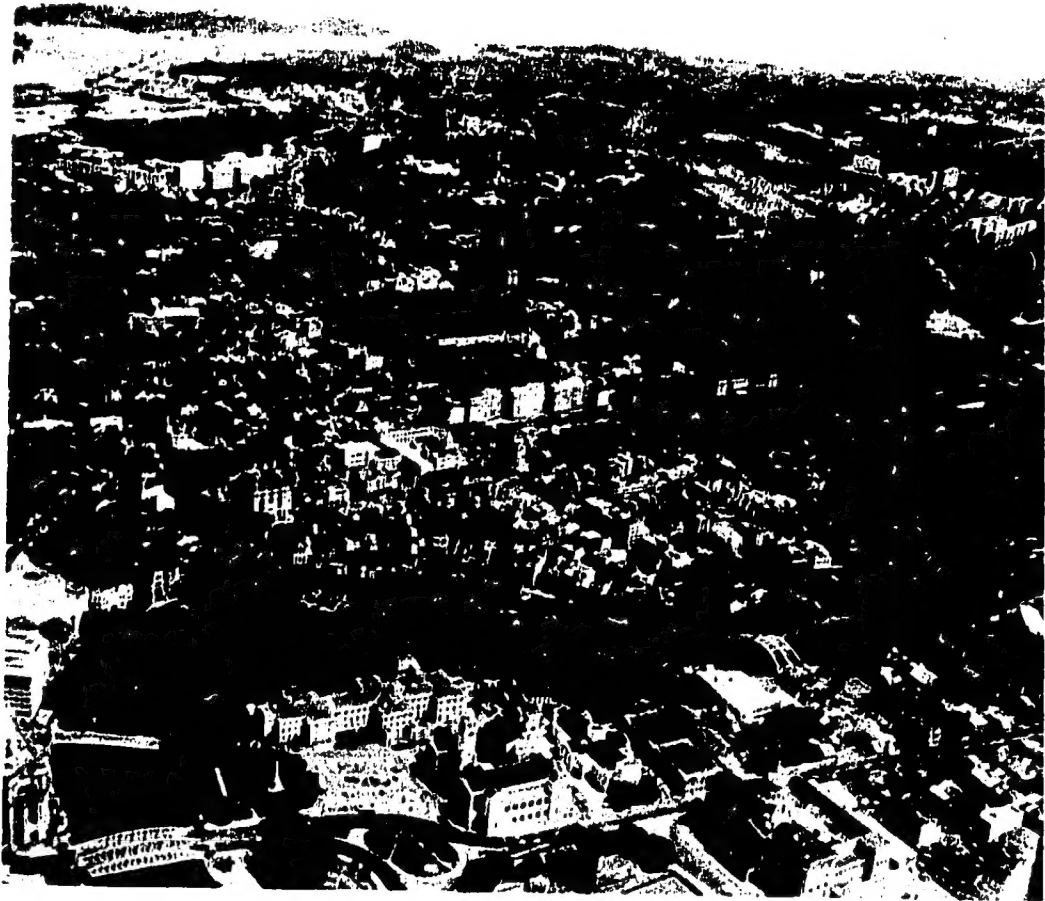
With about 10 percent of the island's labor force unemployed, the withdrawal would be disruptive to Singapore's economy if there were not offsetting factors. Roughly one-fourth of the base workers are Malays and Indians and, by agreement between London and Singapore, they will be discharged first and encouraged to leave the country. Expanding tourism will absorb some of the slack in the service industries, which now cater to British servicemen. About 13,000 of the base employees are supervisors or skilled industrial personnel who should have little problem finding jobs as the bases are converted to non-military uses and the industrial sector continues to expand. The conversion of the Royal Naval Base to a commercial ship repairing concern is already under way, and prospects look bright for turning the airbases into regional aircraft maintenance and repair facilities (see Figure 1). The government's plan to increase local spending substantially over the next four years will help to offset the recessionary influence of the withdrawal.

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ECONOMIC ACTIVITY



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The Setting

1. Singapore, an island country smaller than Hong Kong, has been independent for just over three years. In June 1959 the United Kingdom granted the island internal self-government under Prime Minister Lee Kuan Yew, leader of the Peoples' Action Party (PAP). In 1963, Singapore joined with Malaya and the Borneo States of Sabah and Sarawak to form the Federation of Malaysia. But the racial antagonism between the Malays and the largely Chinese population of Singapore and the increasing friction between Lee and Federation leaders in Kuala Lumpur was too deep, leading Singapore to withdraw from the Federation in August 1965.

2. Traditionally the island has been the leading entrepôt port in Southeast Asia, but this role was changing even before the breakup of Malaysia. The

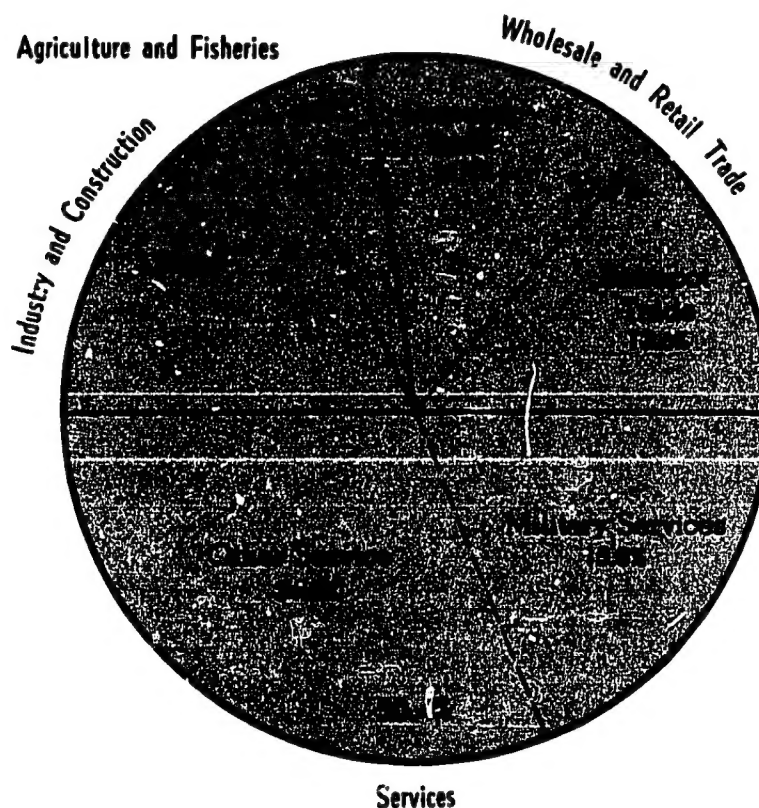
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flow of goods between the less developed countries of the region and the developed countries of the world via Singapore is declining in importance, accounting for only about 13 percent of the country's GDP in 1967 (see Table 1 and Figure 2). Singapore is gradually becoming an entrepôt/manufacturer by processing many of the raw materials which pass through its ports, although the local Chinese businessmen are traditionally traders, and many of them are reluctant to move into manufacturing. But the recent problems with Communist agitators in Hong Kong have encouraged some investors there to examine opportunities in Singapore, and this may help to accelerate investment in manufacturing.

Figure 2

SINGAPORE: GROSS DOMESTIC PRODUCT 1966

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3. Singapore has benefited over the years from a substantial British military presence. The island's officials have long known that the British eventually would leave, and London's announcement in 1967 that British forces east of Suez would be withdrawn by the mid-1970's came as no surprise. Indeed, Singapore's defense planning after the break with Malaysia assumed that the presence of British forces could not be counted on beyond 1975. The shock came with the UK announcement in January 1968 that withdrawal had been moved forward to 1971. After an initial period of threats of reprisal, Singapore began to work out programs to take up the expected slack in the economy.

The UK Military Presence

4. The UK military establishment in Singapore was and is impressive in terms of the number of people and the size of the installations involved. In April 1967 the United Kingdom had 28,800 uniformed personnel, 2,000 civilians, and 3,300 Gurkhas stationed in Singapore. The bases occupy 17,069 acres, or 12 percent of the island's total land area. About 54,000 local personnel were employed in early 1967, including persons employed directly by the bases, locally enlisted personnel (90 percent of whom were Malays not holding Singapore citizenship), domestics, and persons employed by contractors working on the bases. Probably as many more were indirectly dependent on the British for jobs.

5. The direct expenditures attributable to the bases and to UK personnel in Singapore in 1966 (the last year for which complete figures are available) totaled about \$187 million. These expenditures generated roughly 20 percent of national income and represent a valuable source of foreign exchange (see Table 2). Singapore runs a chronic deficit on its balance of trade, which is made up by a surplus in services, consisting largely of the British military expenditures.

Population and Employment Problems

6. Unemployment is Singapore's major economic problem and the greatest potential threat to stability. There are no government statistics on the size of the labor force or the number of unemployed; however, a survey made by the University of Singapore in

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1966 and data from the Labor Exchange suggest that about 60,000 people are now unemployed and that this represents roughly 10 percent of the labor force. Probably at least an equal number are underemployed.

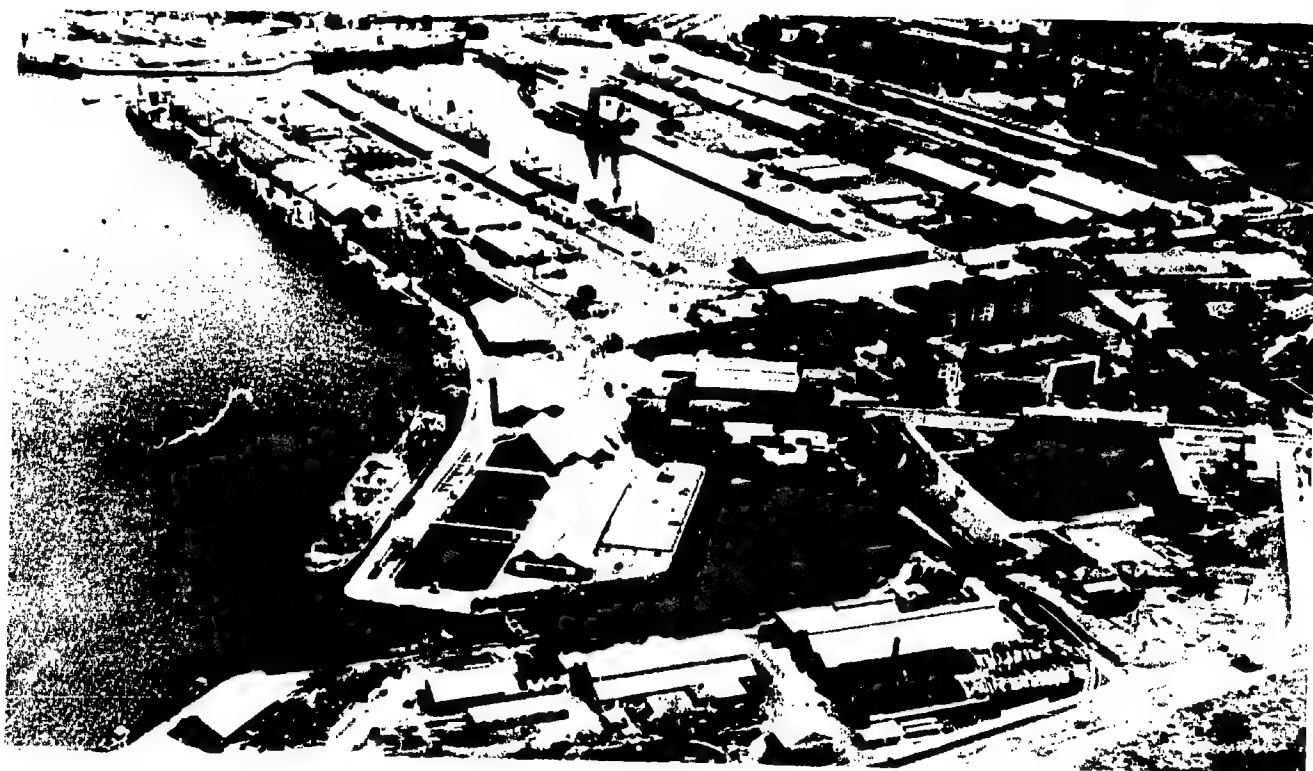
7. After World War II, Singapore's birth rate soared and became one of the world's highest. While population growth remained high throughout most of the 1950's, it has declined from 4.4 percent in 1959 to 2.2 percent in 1967. The government's goal is to reduce the rate of population growth to 1.2 percent by the end of 1970, a goal which may be reached by 1971 or 1972. The reduction in the birth rate should soon begin to ease the burden on Singapore's education system, but for a number of years at least it will not ease the island's major problem of a large number of young people entering the labor force annually (see Table 3).

8. Singapore has an unbalanced age distribution -- more than half of the island's 2 million people are under 20 years of age. Each year, more than 50,000 people reach working age, and the number is expected to swell to 60,000 by 1972. The labor force participation rate in the 15-to-19 age group is 44 percent for males and 25 percent for females (comparable rates for Hong Kong in 1961 were 55 percent and 48 percent). Thus 18,000 to 20,000 young people will be entering the labor force annually between now and 1972. Just to hold unemployment to the present rate, about 70,000 new jobs will have to be created by 1972. Although the economy has grown at an average of 9 percent a year since 1960, the unemployment rate has almost doubled during that time.

Singapore and Malaysia

9. Singapore's domestic market is too small for the development of a viable industrial sector. The Federation with Malaysia was seen as a partial solution to this problem. Even at the time of the 1965 break, both sides promised full economic cooperation, and many hoped a common market might still be formed. But economic cooperation has not developed, and prospects for a common market are dim. Although Malaysia is still Singapore's most important trading partner, accounting for one-fourth of the total, trade has declined since separation. In the first

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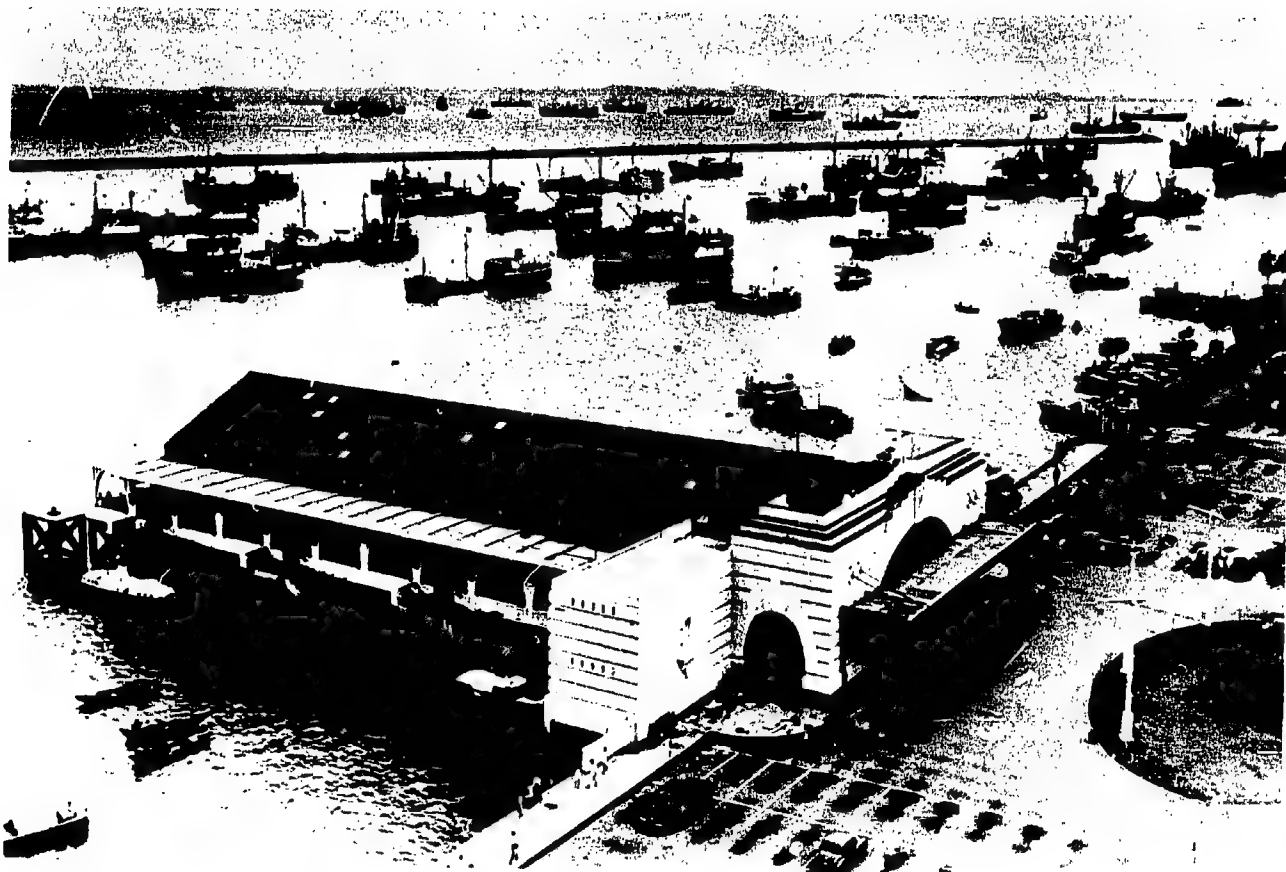


The Singapore Harbor

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In the Foreground, the Singapore Customs Shed

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five months of 1968, Singapore's exports to West Malaysia were down 17 percent and imports 10 percent from the same period in 1965. Trade is expected to continue to decline in relative, if not absolute, terms as Malaysia raises tariff barriers to protect its own processing industries and ports. Singapore traditionally served a large hinterland in West Malaysia with imports from third countries coming via Singapore. Malaysia has been successful in re-directing some of this traffic to West Malaysian ports but has not succeeded in finding other outlets for Malaysian rubber, which continues to be processed in Singapore (see Tables 4, 5, and 6).

10. Aside from a decline in transit trade, Singapore probably has not suffered from its break with the Federation of Malaysia. Economic integration with Malaysia would have had advantages in terms of market size, but the Chinese business community in Singapore would have been restricted in this larger market by the Malay-dominated federal government. Programs to promote economic integration within Malaysia were being implemented very slowly, if at all, because of continuing communal and political rivalries between the member states. Disputes between the federal government and the government of Singapore were intense on questions of economic policy, with each side claiming that the other lacked the proper common market spirit. Disputes centered on such matters as the size of Singapore's financial contribution to the federal government, allocation of Malaysia's quota for textile exports to the United Kingdom, and the establishment of a common external tariff.

11. The dispute over allocation of the textile quota is a good example of a number of federal policies which discriminated against Chinese-dominated Singapore. Under the quota negotiated by the federal government with London in 1965, Malaysia could export annually to the United Kingdom 9.8 million square yards of woven textiles and 7.6 million square yards of made-up goods. The federal government reserved for Malaya the entire quota for woven goods. It also reserved 4.7 million square yards of the made-up goods for Malaya in spite of the fact that no garment manufacturers in Malaya could produce this volume of goods for export. Meanwhile, textile manufacturers in Singapore were being forced to cut back operations and lay off workers.

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Government Policies

12. The failure to achieve a common market with Malaysia has resulted in increased efforts by the Singapore government to attract foreign firms with established international markets. The main investment incentives that Singapore offers are an ideal location from which to tap the Southeast Asian market; a well-developed infrastructure in transportation, communications, and banking; experience in international trade; a stable political and economic situation, including a sound, freely convertible currency; a plentiful, relatively well-educated labor supply; and a favorable tax structure. Singapore must compete for foreign capital with Hong Kong, Taiwan, and to some extent South Korea, all of which offer most of these incentives plus a labor supply which is cheaper and less protected by unions and legislation. Singapore has recently enacted legislation aimed at reducing labor costs and restricting union prerogatives by limiting fringe benefits, reducing overtime, making wage increases and bonuses dependent on productivity, and giving employers a free hand to discharge workers "for cause" and to promote workers without regard to seniority. The change in tone on the part of the government is designed to reassure investors that in Singapore profits are not frowned upon and to remind the unions that the time has come for belt tightening. This is a marked change both for Prime Minister Lee, who started his career in the labor movement, and for a government which came to power through the support of labor.

13. Singapore offers a number of tax breaks designed to encourage investment. Most new firms enjoy a tax holiday of two to five years. To encourage established firms to expand, profits derived from expansion are tax exempt for a period of three to five years. The tax structure was modified in 1967 to favor firms manufacturing for export. Profits derived from the export of locally produced goods are taxed at only 4 percent instead of the normal rate of 40 percent. To encourage the flow of capital into Singapore (especially from Hong Kong) the tax rate on interest earned on deposits in Singapore banks by nonresidents was reduced from 40 to 10 percent in 1967. An additional attractive feature of Singapore to overseas Chinese investors from Hong Kong and Indonesia is that investors are eligible for citizenship.

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Singapore: Three-Story Low-Cost Workmen's Flats

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Singapore: Kallang Basin Slum Area to be Redeveloped

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Implications of the UK Withdrawal

14. The withdrawal of British forces which began last year is scheduled to be completed by the end of 1971. Between May 1967 and July 1968, about 6,500 civilian employees and 950 enlisted personnel lost their jobs. About one-fourth of all base employees are Indians and Malays who are not citizens of Singapore. By agreement between the UK and Singapore, these persons will be released first and encouraged to leave the island. The United Kingdom has agreed to make a payment to each worker who loses his job because of withdrawal, and this money will go into a fund set up by the government of Singapore. Citizens will eventually be able to draw the full amount, but noncitizens will be able to draw only two-thirds unless they leave the island permanently. About 13,000 of the local base civilians are supervisors and skilled industrial personnel who will have little problem finding employment as the bases are converted and the industrial sector in Singapore continues to expand. Some of the slack in the large services sector, which caters to the British servicemen, will be taken up by the expanding tourist trade. The number of visitors arriving in Singapore was up 60 percent in 1967, to about 205,000. The expansion is continuing in 1968, with the number of arrivals in the first four months up 31 percent above the same period in 1967.

15. The United Kingdom will provide \$120 million to help offset the money Singapore loses when the British withdraw. Beginning this year, 75 percent of the aid distributed over the next five years will be in the form of an interest-free loan, repayable over 25 years with a seven-year grace period. The balance will be an outright grant. London and Singapore have already agreed on the initial allocation of \$32.7 million for the period April 1968 to March 1969. Specific projects include: conversion of the Royal Naval Dockyard, \$2.9 million; vocational training, \$3.3 million; purchase of British machinery and equipment, \$9.8 million; harbor modernization, \$1.8 mil-

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profitable commercial enterprises. The conversion of the Royal Naval Dockyard is already under way, and offers have gone out to 3,000 of the 5,000 skilled and semi-skilled workers to remain on the job when the yard becomes commercial at the end of this year. The ship repairing business has been booming in Singapore, and prospects are bright for the converted base to be a successful enterprise. There are also prospects for converting the Royal Air Force bases. Both US and Australian investors have expressed an interest in converting the bases to regional aircraft maintenance and repair facilities.

Singapore's Plans for Adjustment

17. From now until the end of 1971, when the British complete the withdrawal, there will be a progressive reduction in the UK's military expenditures in Singapore. For its part, Singapore will adjust its fiscal and monetary policy to smooth the transition. In March the Minister of Finance announced plans to increase government spending by \$312 million during the transition period to offset the recessionary influence of declining British expenditures. Singapore expects to raise the \$312 million for additional government spending by official overseas aid and loans (\$93 million), floating loans on overseas money markets (\$49 million), increased local taxation and borrowing (\$114 million), and drawing down its foreign reserves (\$56 million). The official overseas aid portion is already oversubscribed (the United Kingdom alone has promised \$120 million). The \$49 million figure for private foreign loans is well within Singapore's capacity to raise, considering the island's high international credit standing (see Table 7). The level of official foreign reserves stood at more than \$490 million at the end of 1967 and will only have to be reduced by about 10 percent in order to raise the \$56 million from that source (see Table 8).

18. The planned \$312 million increase in government spending will be divided between defense and

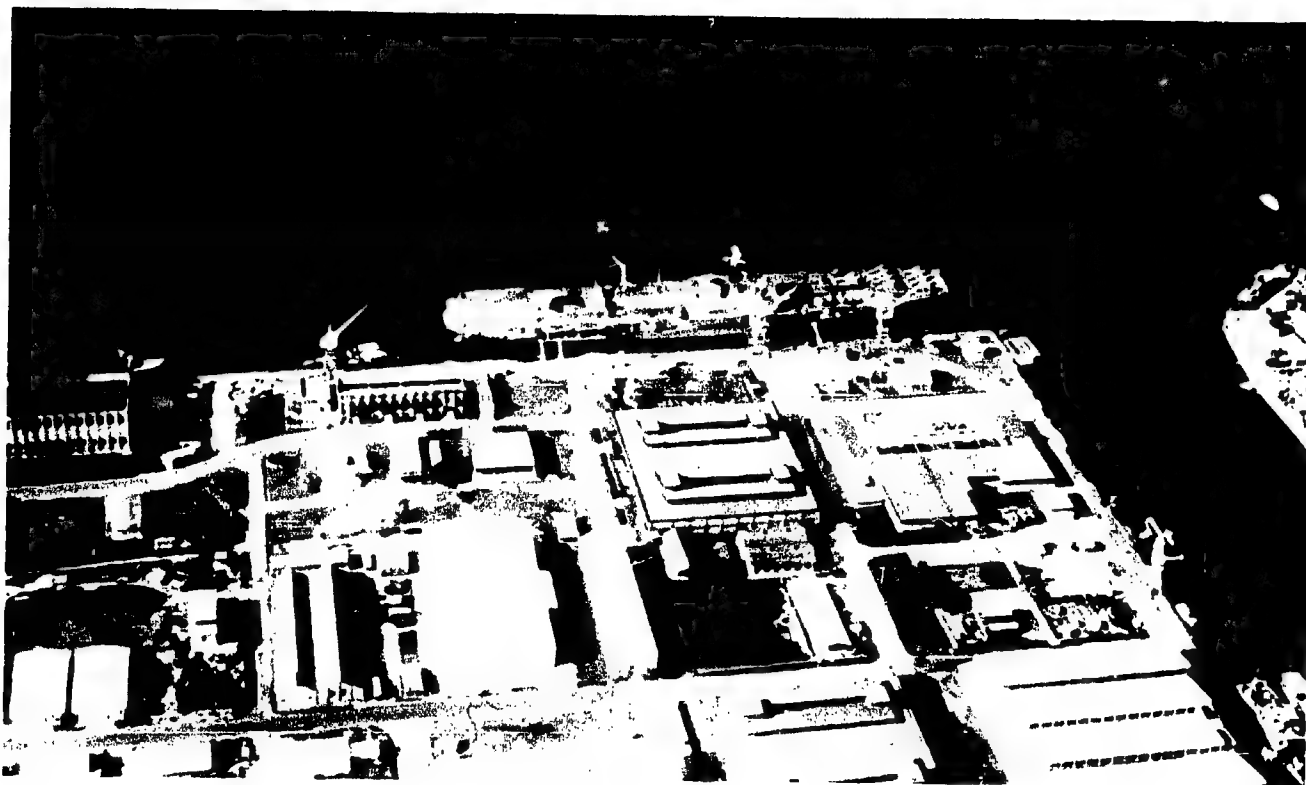
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for the middle and late 1970's will be advanced several years, including express highways, a second large industrial complex, land reclamation, and an increase in housing construction from the 12,000 units per year previously planned to 16,500 units per year. In addition, Singapore hopes to increase private investment by \$65 million over the four-year period by accelerating the construction of tourist hotels and by loan guarantees and equity participation. Some \$20 million of the increased government expenditures has been allotted for this purpose. To encourage increased private construction, interest rates on approved private buildings started during the period 1968-71 will be subsidized sufficiently to reduce the effective interest rate to between 2½ and 4 percent throughout the life of the mortgage.

Prospects

19. The British pullout will not cause major disruptions in Singapore's economy, because the conversion of the bases, the government's expansionary monetary and fiscal policy, and the infusion of UK aid will cushion the impact. Aided by foreign capital, Singapore's economy is growing rapidly, and the British withdrawal may slow but probably will not stop Singapore's economic development. On balance, the economy will probably expand at a rate of 8 percent or more for the next few years. Unemployment, the island's major economic problem, will, of course, be aggravated by the withdrawal. But conversion of bases, the expected rise in tourism, and Singapore's plans to enlarge its military establishment (16,000 young people are to be inducted each year) should keep unemployment close to present levels.

20. Investors seem to be confident about Singapore's future after the British leave, and the government intends to maintain that confidence. An increased inflow of investors specializing in labor-intensive industry would go a long way toward solving Singapore's unemployment problem. There is mounting evidence that such an inflow may take place in



The Singapore Naval Base

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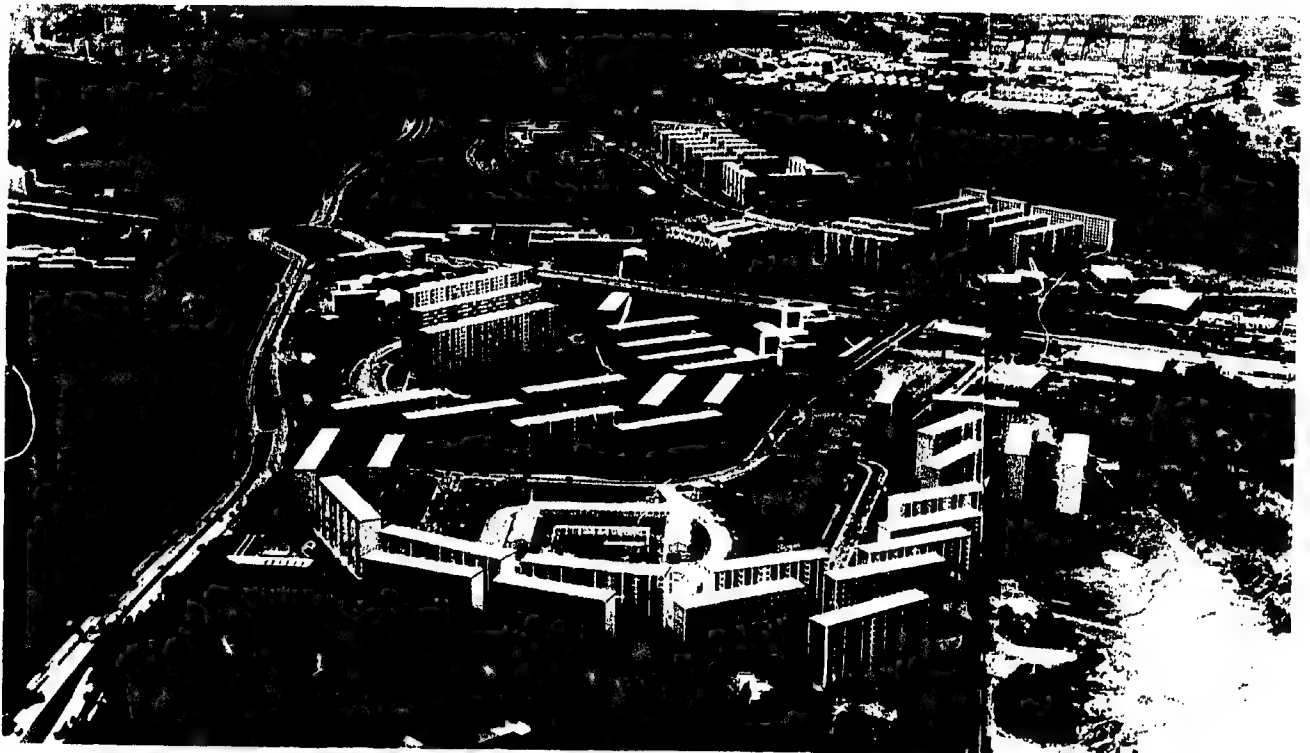


Singapore: The Queen's Drydock

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Singapore: The Queenstown Housing Project

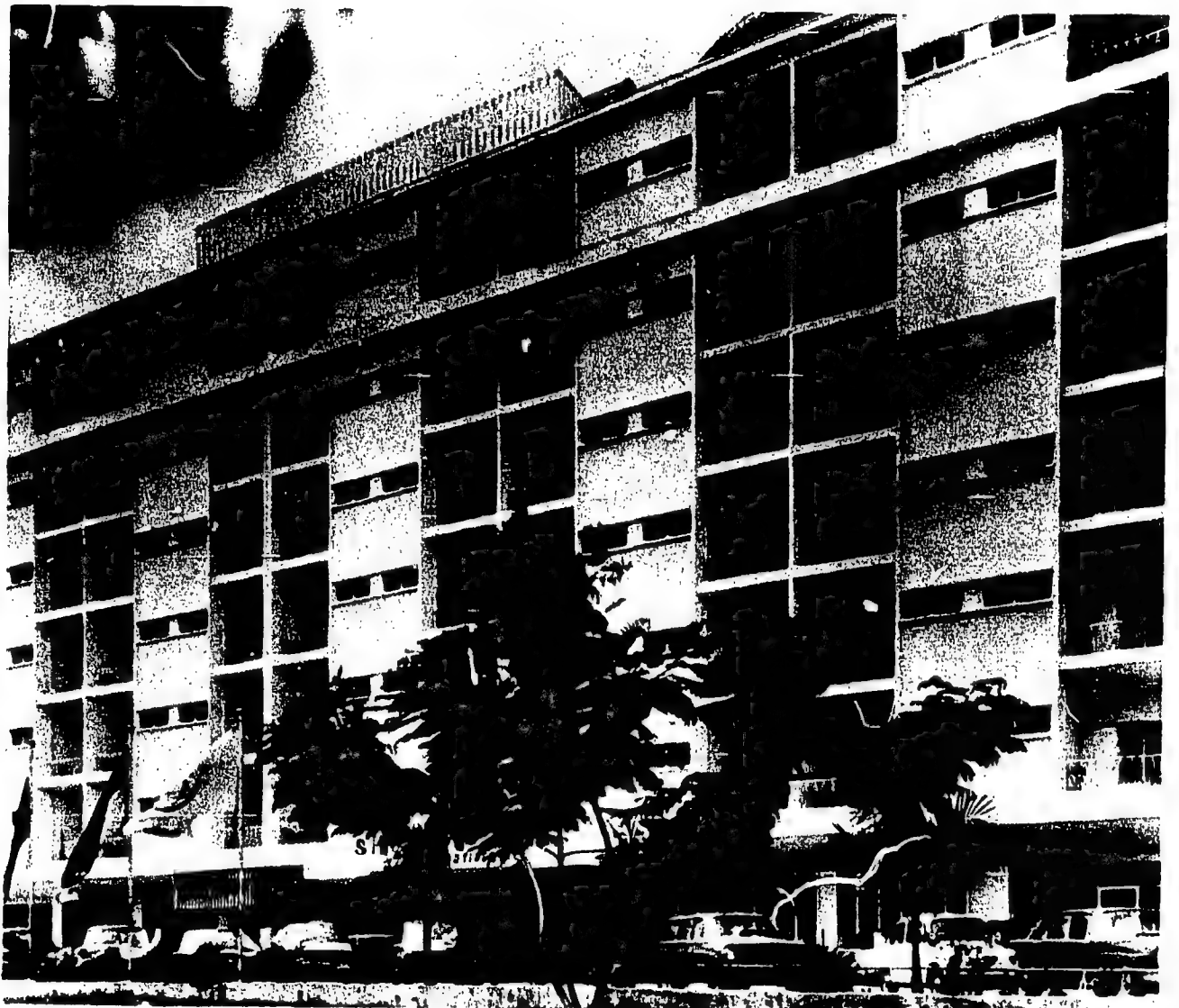
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Singapore: The Hotel Singapura Intercontinental

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Table 1

Singapore: Estimates of Gross Domestic Product, by Sector of origin ^{a/}
1960-66

	1960		1961		1962		1963		1964		1965		1966	
	Million US \$	Percent	Million US \$	Percent	Million US \$	Percent	Million US \$	Percent	Million US \$	Percent	Million US \$	Percent	Million US \$	Percent
Agriculture and fisheries	40.9	6.0	44.6	6.1	45.5	5.9	48.5	5.5	46.9	5.3	48.2	4.8	54.1	4.9
Mining and quarrying	1.3	0.2	1.3	0.2	1.7	0.2	2.0	0.2	2.3	0.3	2.0	0.2	2.3	0.2
Manufacturing	48.8	7.3	59.4	8.1	62.4	8.1	74.3	8.5	83.5	9.5	99.7	10.0	116.8	10.6
Construction	13.9	2.1	21.8	3.0	23.4	3.0	31.4	3.6	37.6	4.3	43.2	4.3	42.6	3.8
Electricity, gas, and other services	16.8	2.5	17.8	2.4	19.5	2.5	19.8	2.3	22.4	2.5	22.4	2.2	26.7	2.4
Wholesale and retail trade	217.5	32.6	235.3	32.2	245.9	31.8	297.7	34.0	248.5	28.2	270.0	27.0	306.3	27.7
Entrepôt	128.7	19.3	131.4	18.0	134.0	17.3	159.7	18.3	109.2	12.4	121.1	12.1	149.8	13.5
Domestic	88.8	13.3	104.0	14.2	111.9	14.5	138.0	15.8	139.3	15.8	148.8	14.9	156.4	14.1
Ownership of dwellings	30.7	4.6	33.3	4.6	34.3	4.4	36.3	4.2	38.9	4.4	42.6	4.3	46.9	4.2
Government services	35.0	5.3	47.5	6.5	54.1	7.0	62.4	7.1	63.0	7.2	70.6	7.1	88.4	8.0
Military services	92.1	13.8	92.7	12.7	99.3	12.9	106.6	12.2	136.0	15.4	171.3	17.1	174.6	15.8
Other services	171.0	25.7	177.9	24.3	186.5	24.1	195.7	22.4	201.0	22.8	231.0	23.1	247.9	22.4
Tourism	10.2	1.5	10.6	1.4	13.2	1.7	18.2	2.1	20.1	2.3	21.5	2.1	27.4	2.5
Other	160.7	24.1	167.3	22.9	173.3	22.4	177.6	20.3	180.9	20.5	209.6	20.9	220.5	19.9
Statistical discrepancy	-1.7		26.2		66.7		34.5		9.7		-42.3		-10.6	
GDP at factor cost	666.3		757.8		839.3		909.2		889.8		958.7		1,096.0	

^{a.} Because of rounding, components may not add to the totals shown.

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Table 2

Estimated Contribution of UK Bases
to Singapore's Gross Domestic Product
1966

	Million US \$
Expenditures	187
Wages and salaries to local civilians	42
Expenditures of UK military personnel	79
Local base expenditures	57
Other	9
Import content of local purchases	-53
Direct contributions	134
Indirect contribution	<u>87</u>
Total <u>a/</u>	221

a. Equal to 20 percent of GDP.

Table 3

Unemployment in Singapore a/
1966

Age Group	Previously Employed	Never Previously Employed	Unemployed	
			Total	Percent of Total
10 to 19	4,061	18,545	22,606	42.9
20 to 29	8,473	8,814	17,287	32.8
30 to 39	4,228	844	5,072	9.6
40 and over	7,115	586	7,701	14.6
Total	23,877	28,789	52,666	100.0

a. Based on a survey of sample households.

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Table 4

Singapore: Foreign Trade, by Major Commodities a/
1963 and 1967

	1963		1967	
	Million US \$	Percent of Total	Million US \$	Percent of Total
<u>Exports</u>				
Crude rubber	318	28	246	19
Coffee	31	3	41	3
Pepper	19	2	20	2
Cotton piece goods	27	2	17	2
Sawn timber	10	1	16	1
Pineapple	12	1	15	1
Rice	29	2	14	1
Palm oil	7	1	13	1
Other	682	60	889	70
<i>Total</i>	<i>1,135</i>	<i>100</i>	<i>1,271</i>	<i>100</i>
<u>Imports</u>				
Crude rubber	266	19	244	15
Synthetic fabrics	29	2	49	3
Rice	56	4	46	3
Cotton piece goods	41	3	45	3
Coffee	14	1	29	2
Pepper	17	1	21	1
Palm oil	8	1	14	1
Pineapple	9	1	14	1
Other	958	68	1,130	71
<i>Total</i>	<i>1,398</i>	<i>100</i>	<i>1,592</i>	<i>100</i>

a. Data reflect the dominance of Singapore's role as an entrepôt, inasmuch as only a small portion of the major commodities involved in Singapore's foreign trade are produced or consumed locally. For data on domestic exports and retained imports, see Table 5.

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Table 5
Foreign Trade of Singapore
1960-67

	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964 a/</u>	<u>1965 a/</u>	<u>1966 a/</u>	<u>1967</u>
	Value (Million US \$)							
Total exports	1,136	1,081	1,117	1,135	906	982	1,103	1,271
Of which: Domestic exports	71	74	82	91	97	113	130	N.A.
Total imports	1,332	1,295	1,319	1,398	1,137	1,244	1,329	1,592
Of which: Retained imports	423	447	469	568	529	591	614	N.A.
	Index (1960 = 100)							
Total exports	100	95	98	100	80	86	97	112
Of which: Domestic exports	100	104	115	128	137	159	183	N.A.
Total imports	100	97	99	105	85	93	100	120
Of which: Retained imports	100	106	111	134	125	140	145	N.A.

a. Excluding Indonesia.

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Table 6

Foreign Trade of Singapore, by Major Countries
1967

	Exports	
	Million US \$	Percent of Total
Malaysia	359	28
Of which: West Malaysia <u>a/</u>	(270)	(21)
Indonesia	131	10
South Vietnam	102	8
United States	80	6
United Kingdom	69	5
Japan	51	4
Other	479	39
<i>Total</i>	1,271	100
	Imports	
	Million US \$	Percent of Total
Malaysia	350	22
Of which: West Malaysia <u>a/</u>	(274)	(17)
Japan	179	11
Indonesia	152	10
Communist China	125	8
United Kingdom	116	7
United States	80	5
Other	590	37
<i>Total</i>	1,592	100

a. Formerly Malaya.

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Table 7

Singapore: External Medium-Term
and Long-Term a/ Public Debt Outstanding
as of 31 December 1967

	Thousand US \$	
	<u>Total</u>	<u>Disbursed</u>
Total external public debt	<u>83,109</u>	<u>33,465</u>
Debt repayable in foreign currency	74,663	32,660
IBRD loans	71,365	29,362
UK government loans	3,298	3,298
Debt repayable in local currency	8,446	805
Suppliers credits	8,446	805

a. Debt with an original or extended maturity of one year or more.

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Table 8
Foreign Exchange Reserves of Singapore
1960-67

	Million US \$							
	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u> a/
Singapore's estimated share of Malay-Borneo Currency Board's exchange assets	90.2	88.4	87.6	88.8	89.5	89.9	98.3	162.1 b/
Singapore government	110.5	131.9	167.5	194.3	179.8	159.7	171.3	278.1
Government agencies and other public authorities	47.4	70.2	72.1	63.2	65.6	55.3	65.8	51.0
Official reserves	248.1	290.5	327.2	346.3	334.9	304.9	335.4	491.3
Commercial bank's foreign exchange assets	169.0	159.7	174.3	162.5	185.6	236.1	243.5	170.3
Gross reserves	417.1	450.2	501.5	508.8	520.5	541.0	578.9	661.5
Less commercial bank's foreign exchange liabilities	104.8	113.3	109.0	102.6	151.1	207.3	203.6	109.0
Net reserves	312.3	336.9	392.5	406.2	369.4	333.7	375.3	552.5

a. Data for 1967 is not comparable with other years, because Singapore's share of the Currency Board's assets was underestimated up to that time. Thus, of the apparent increase of \$64 million, perhaps \$60 million is a statistical adjustment. It should also be noted that the sharp increase in Singapore government foreign assets largely represents the end result of a windfall inflow of capital from Hong Kong in 1967 as well as a shift out of Malaysia into Singapore treasury bills in 1967.

b. Including \$138.3 million foreign assets of the Singapore Currency Board.